

AUDITING PROCEDURES REPORT

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Local Government Type [] City [] Township [] Village [x] Other		Local Government Name City of Battle Creek, Kellogg Arena Fund		County Calhoun	
Audit Date June 30, 2005		Opinion Date September 2, 2005		Date Accountant Report Submitted to State: November 9, 2005	

We have audited the financial statements of this local unit of government and rendered an opinion on financial statements prepared in accordance with the Statements of the Governmental Accounting Standards Board (GASB) and the *Uniform Reporting Format for Financial Statements for Counties and Local Units of Government in Michigan* by the Michigan Department of Treasury.

We affirm that:

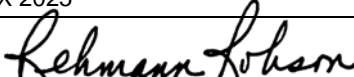
1. We have complied with the *Bulletin for the Audits of Local Units of Government in Michigan* as revised.
2. We are certified public accountants registered to practice in Michigan.

We further affirm the following. "Yes" responses have been disclosed in the financial statements, including the notes, or in the report of comments and recommendations

You must check the applicable box for each item below.

- | | | | | | |
|-----|-----|-----|----|----|--|
| [] | Yes | [x] | No | 1. | Certain component units/funds/agencies of the local unit are excluded from the financial statements. |
| [] | Yes | [x] | No | 2. | There are accumulated deficits in one or more of this unit's unreserved fund balances/retained earnings (P.A. 275 of 1980). |
| [x] | Yes | [] | No | 3. | There are instances of non-compliance with the Uniform Accounting and Budgeting Act (P.A. 2 of 1968, as amended). |
| [] | Yes | [x] | No | 4. | The local unit has violated the conditions of either an order issued under the Municipal Finance Act or its requirements, or an order issued under the Emergency Municipal Loan Act. |
| [] | Yes | [x] | No | 5. | The local unit holds deposits/investments which do not comply with statutory requirements. (P.A. 20 of 1943, as amended [MCL 129.91], or P.A. 55 of 1982, as amended [MCL 38.1132]). |
| [] | Yes | [x] | No | 6. | The local unit has been delinquent in distributing tax revenues that were collected for another taxing unit. |
| [] | Yes | [x] | No | 7. | The local unit has violated the Constitutional requirement (Article 9, Section 24) to fund current year earned pension benefits (normal costs) in the current year. If the plan is more than 100% funded and the overfunding credits are more than the normal cost requirement, no contributions are due (paid during the year). |
| [] | Yes | [x] | No | 8. | The local unit uses credit cards and has not adopted an applicable policy as required by P.A. 266 of 1995 (MCL 129.241). |
| [] | Yes | [x] | No | 9. | The local unit has not adopted an investment policy as required by P.A. 196 of 1997 (MCL 129.95). |

We have enclosed the following:	Enclosed	To Be Forwarded	Not Required
The letter of comments and recommendations.	X		
Reports on individual federal financial assistance programs (program audits).			X
Single Audit Reports (ASLGU).			X

Certified Public Accountant (Firm Name) REHMANN ROBSON GERALD J. DESLOOVER, CPA			
Street Address 5800 GRATIOT, PO BOX 2025		City SAGINAW	State MI
Accountant Signature 		Zip 48605	

**CITY OF BATTLE CREEK
KELLOGG ARENA FUND**

Battle Creek, Michigan

FINANCIAL STATEMENTS

**For The Year Ended
June 30, 2005**



REHMANN ROBSON

Certified Public Accountants

CITY OF BATTLE CREEK KELLOGG ARENA FUND

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REHMANN ROBSON

Certified Public Accountants

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INDEPENDENT AUDITORS' REPORT

September 2, 2005

To the Honorable Mayor and
Members of the City Council of the
City of Battle Creek, Michigan and
Management of the Kellogg Arena Fund
Battle Creek, Michigan

We have audited the accompanying financial statements of the ***KELLOGG ARENA FUND, a special revenue fund of the City of Battle Creek, Michigan***, as of and for the year ended June 30, 2005, as listed in the table of contents. These financial statements are the responsibility of the Kellogg Arena Fund's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 1, the financial statements present only the Kellogg Arena Fund and do not purport to, and do not present fairly the financial position of the City of Battle Creek, Michigan as of June 30, 2005, and the changes in its financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Kellogg Arena Fund as of June 30, 2005, and the changes in financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The Kellogg Arena Fund has not presented Management's Discussion and Analysis as required supplementary information. The Governmental Accounting Standards Board has determined that such information is necessary to supplement, although not required to be part of the basic financial statements.

Our audit was performed for the purpose of forming an opinion on the financial statements taken as a whole. The supplemental schedule listed in the table of contents is presented for purposes of additional analysis and is not a required part of the financial statements of the Kellogg Arena Fund. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly presented in all material respects in relation to the financial statements taken as a whole.

A handwritten signature in black ink, reading "Lehmann Lobson". The signature is written in a cursive, flowing style.

FINANCIAL STATEMENTS

KELLOGG ARENA FUND

Balance Sheet

June 30, 2005

ASSETS

Assets

Cash and cash equivalents	\$ 1,009,917
Investments	190,404
Accounts receivable	426,038
Inventories	12,170
Prepaid items	8,910

TOTAL ASSETS

\$ 1,647,439

LIABILITIES AND FUND BALANCE

Liabilities

Accounts payable and accrued liabilities	\$ 850,734
Unearned revenue	87,146
Total liabilities	<u>937,880</u>

Fund balance

Reserved:	
Reserved for inventories	12,170
Reserved for prepaid items	8,910
Reserved for renovation project	366,151
Unreserved, undesignated	<u>322,328</u>
Total fund balance	<u>709,559</u>

TOTAL LIABILITIES AND FUND BALANCE

\$ 1,647,439

The accompanying notes are an integral part of these financial statements.

KELLOGG ARENA FUND
Statement of Revenues, Expenditures
and Changes in Fund Balance - Amended Budget and Actual
For the Year Ended June 30, 2005

	<u>Amended Budget</u>	<u>Actual</u>	<u>Over (Under) Budget</u>
Revenues			
Events	\$ 872,770	\$ 755,251	\$ (117,519)
Concessions	160,377	185,630	25,253
Contract	306,695	485,098	178,403
Novelty	31,851	7,788	(24,063)
Bar	91,371	88,386	(2,985)
Pro Shop	-	4,865	4,865
Other	38,657	39,630	973
Grant - Kellogg Foundation	<u>-</u>	<u>1,750,000</u>	<u>1,750,000</u>
 Total revenues	 <u>1,501,721</u>	 <u>3,316,648</u>	 <u>1,814,927</u>
 Expenditures			
Operating	720,105	834,387	114,282
Building	254,727	266,494	11,767
Administrative	547,889	528,810	(19,079)
Renovation	<u>-</u>	<u>3,153,849</u>	<u>3,153,849</u>
 Total expenditures	 <u>1,522,721</u>	 <u>4,783,540</u>	 <u>3,260,819</u>
 Revenues under expenditures	 <u>(21,000)</u>	 <u>(1,466,892)</u>	 <u>(1,445,892)</u>
 Other financing sources			
Transfer from City of Battle Creek	-	1,770,000	1,770,000
Transfer from Battle Creek Downtown Development Authority	<u>21,000</u>	<u>75,000</u>	<u>54,000</u>
 Total other financing sources	 <u>21,000</u>	 <u>1,845,000</u>	 <u>1,824,000</u>
 Net change in fund balance	 -	 378,108	 378,108
 Fund balance, beginning of year	 <u>331,451</u>	 <u>331,451</u>	 <u>-</u>
 Fund balance, end of year	 <u><u>\$ 331,451</u></u>	 <u><u>\$ 709,559</u></u>	 <u><u>\$ 378,108</u></u>

The accompanying notes are an integral part of these financial statements.

KELLOGG ARENA FUND

Notes to Financial Statements

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the Kellogg Arena Fund (the “Fund”), a special revenue fund of the City of Battle Creek, Michigan, have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The more significant of the fund’s accounting policies are described below.

Reporting Entity – These financial statements represent the financial condition and the results of operations of a special revenue fund of the City of Battle Creek, Michigan (the “City”) and are an integral part of that reporting entity. The Fund is not a component unit of the City or any other reporting entity, as defined by GASB Statement No. 14, *The Financial Reporting Entity*.

The Fund is used to account for the activities of two City-owned public entertainment and recreation facilities: the Kellogg Arena and The Rink, which is an enclosed ice rink. Both facilities are managed and operated by the Cereal City Development Corporation (CCDC), a legally separate nonprofit organization, pursuant to an agreement with the City. CCDC is not a component unit of the City or any other reporting entity, as defined by GASB Statement No. 14, since it is not a unit or instrumentality of government.

Basis of Accounting – The City uses a special revenue fund (i.e., a separate accounting entity with a self-balancing set of accounts, using the modified-accrual basis of accounting) to report the Fund’s financial position and results of operations. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain governmental functions and activities.

Deposits and Investments – The Fund’s cash and cash equivalents consist of cash on hand, demand deposits and short-term investments with original maturities of three months or less from the date of acquisition.

State statutes authorize local governments to deposit in the accounts of federally insured banks, credit unions, and savings and loan associations, and to invest in obligations of the U.S. Treasury, certain commercial paper, repurchase agreements, bankers acceptances, and mutual funds composed of otherwise legal investments.

KELLOGG ARENA FUND

Notes to Financial Statements

Receivables - Receivables consist primarily of fees and other such charges for services to third parties that rent the facilities for conventions, meetings and other events and are reported net of amounts estimated to be uncollectible.

Inventories - Inventories are valued at cost using the first-in/first-out (FIFO) method.

Prepaid Items - Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items.

Revenue Recognition - Revenues from certain facility activities are recognized at the time the related events occur. Accordingly, advanced ticket sales and deposits paid by customers prior to the date of event are reported as unearned revenues.

Compensated Absences – Employees are permitted to accumulate earned but unused vacation. A liability for the value of unused vacation is reported in governmental funds only if they have matured, for example, as a result of employee resignations or terminations.

Fund Equity - Reservations of fund balance represent amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. Designations of fund balance, if any, represent tentative management plans that are subject to change.

Budgetary Information - The Fund is under formal budgetary control and its budget is prepared on the same modified accrual basis used to reflect actual results. The Fund follows the City budget process in establishing the budgetary data reflected in the financial statements:

- CCDC submits a proposed budget to the City Manager. After review and approval, the City Manager submits a recommended operating budget to the City Commission. Public hearings are held to obtain taxpayer comments. The budget is legally adopted through a City Commission resolution prior to the beginning of the budgetary year.
- The budget is adopted on a basis consistent with generally accepted accounting principles. Budgeted amounts are as originally adopted or amended by the City Commission during the year. Individual amendments, if any, were not material in relation to the original appropriations.

The budget is adopted at the fund level and unfavorable variances at this level of legal control are displayed on the Statement of Revenues, Expenditures and Changes in Fund Balance – Budget and Actual.

KELLOGG ARENA FUND

Notes to Financial Statements

2. DEPOSITS AND INVESTMENTS

Deposits – At year-end, the carrying amount of the Fund’s deposits was \$994,767 (total cash and cash equivalents of \$1,009,917 includes \$15,150 of petty cash) and the bank balance was \$986,134. Of the bank balance, \$100,000 was covered by federal depository insurance; the remaining balance of \$886,134 was uninsured and uncollateralized.

Investments – At year-end, the carrying amount and fair value of the Fund’s investments were \$190,404 and consisted of money market mutual funds composed of otherwise legal investments. The Fund’s investments in 2a-7 like money market accounts are not subject to custodial credit risk or interest rate risk, nor are the funds rated by a national recognized rating organization.

3. RISK MANAGEMENT

The Fund is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; and natural disasters for which the Fund carries commercial insurance. The Fund has had no settled claims resulting from these risks that exceeded its commercial coverage in any of the past three fiscal years.

4. DEFINED CONTRIBUTION PENSION PLAN

The Fund has a defined contribution pension plan covering substantially all full-time employees who have completed one year of employment. The employer reserves the right to amend or terminate the plan at any time. The Fund contributes 15% of participating employees’ annual compensation to the plan. There is no employee contribution requirement. Employer contributions for the year ended June 30, 2005 were \$57,856.

5. EXCESS OF EXPENDITURES OVER APPROPRIATIONS

State statutes provide that a local unit shall not incur expenditures in excess of the amount appropriated. The approved budgets of the Fund were adopted on a fund level basis, although budget and actual information in the fund financial statements have been presented at a level of detail greater than the level of legal budgetary control.

During the year ended June 30, 2005, the Fund incurred expenditures in excess of the amounts appropriated at the legal level of budgetary control in the following:

	<u>Budget</u>	<u>Actual</u>	<u>Over Budget</u>
Kellogg Arena Fund	\$ 1,522,721	\$ 4,783,540	\$ 3,260,819

KELLOGG ARENA FUND

Notes to Financial Statements

6. COMMITMENT

At year end, the Fund had a commitment for the renovation project of \$1,223,877.

* * * * *

SUPPLEMENTAL SCHEDULE

KELLOGG ARENA FUND
Schedule of Revenues and Expenditures by Facility - Amended Budget and Actual
For the Year Ended June 30, 2005

	Kellogg Arena		
	Amended Budget	Actual	Over (Under) Budget
Revenues			
Events	\$ 623,560	\$ 515,822	\$ (107,738)
Concessions	137,718	160,956	23,238
Contract	306,695	485,098	178,403
Novelty	31,851	7,788	(24,063)
Bar	91,371	88,386	(2,985)
Pro Shop	-	-	-
Other	37,857	38,830	973
Grant - Kellogg Foundation	-	1,750,000	1,750,000
	<hr/>	<hr/>	<hr/>
Total revenues	1,229,052	3,046,880	1,817,828
	<hr/>	<hr/>	<hr/>
Expenditures			
Operating:			
Events	282,758	251,487	(31,271)
Concessions	60,095	72,724	12,629
Contract	300,681	458,720	158,039
Novelty	24,076	1,057	(23,019)
Bar	37,975	31,869	(6,106)
Pro Shop	-	-	-
Building	181,028	193,849	12,821
Administrative	425,902	403,891	(22,011)
Renovation	-	3,153,849	3,153,849
	<hr/>	<hr/>	<hr/>
Total expenditures	1,312,515	4,567,446	3,254,931
	<hr/>	<hr/>	<hr/>
Revenues over (under) expenditures	(83,463)	(1,520,566)	(1,437,103)
	<hr/>	<hr/>	<hr/>
Other financing sources			
Transfer from City of Battle Creek	-	1,770,000	1,770,000
Transfer from Battle Creek Downtown Development Authority	21,000	75,000	54,000
	<hr/>	<hr/>	<hr/>
Total other financing sources	21,000	1,845,000	1,824,000
	<hr/>	<hr/>	<hr/>
Net change in fund balance	\$ (62,463)	\$ 324,434	\$ 386,897
	<hr/>	<hr/>	<hr/>

The Rink		
Amended Budget	Actual	Over (Under) Budget
\$ 249,210	\$ 239,429	\$ (9,781)
22,659	24,674	2,015
-	-	-
-	-	-
-	-	-
-	4,865	4,865
800	800	-
-	-	-
272,669	269,768	(2,901)
-	-	-
14,520	16,480	1,960
-	-	-
-	-	-
-	-	-
-	2,050	2,050
73,699	72,645	(1,054)
121,987	124,919	2,932
-	-	-
210,206	216,094	5,888
62,463	53,674	(8,789)
-	-	-
-	-	-
-	-	-
\$ 62,463	\$ 53,674	\$ (8,789)



REHMANN ROBSON

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September 2, 2005

To the Members of the City Council of the City of Battle Creek
and Management of the Kellogg Arena Fund
Battle Creek, Michigan

We have audited the financial statements of the ***Kellogg Arena Fund, a special revenue fund of the City of Battle Creek, Michigan***, as of and for the year ended June 30, 2005, and have issued our report thereon dated September 2, 2005. Professional standards require that we provide you with the following information related to your audit.

Our Responsibility Under Generally Accepted Auditing Standards

As stated in our engagement letter dated July 15, 2005, our responsibility, as described by professional standards, is to plan and perform our audit to obtain reasonable, but not absolute, assurance that the general purpose financial statements are free of material misstatement and are fairly presented in accordance with accounting principles generally accepted in the United States of America. Because of the concept of reasonable assurance and because we did not perform a detailed examination of all transactions, there is a risk that material errors, fraud, or other illegal acts may exist and not be detected by us.

As part of our audit, we considered the internal control of the Kellogg Arena Fund. Such considerations were solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control.

Significant Accounting Policies

Management has the responsibility for selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we will advise management about the appropriateness of accounting policies and their application. The significant accounting policies used by the Kellogg Arena Fund are described in Note 1 to the general purpose financial statements. No new accounting policies were adopted and the application of existing policies was not changed during the fiscal year ended June 30, 2005. We noted no transactions entered into by the Kellogg Arena Fund during the year that were both significant and unusual, and of which, under professional standards, we are required to inform you, or transactions for which there is a lack of authoritative guidance or consensus.

Accounting Estimates

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the general purpose financial statements and because of the possibility that future events affecting them may differ significantly from those expected. There were no significant accounting estimates made for the year ended June 30, 2005.

Significant Audit Adjustments

For purposes of this letter, professional standards define a significant audit adjustment as a proposed correction of the general purpose financial statements that, in our judgment, may not have been detected except through our auditing procedures. These adjustments may include those proposed by us but not recorded by the Kellogg Arena Fund that could potentially cause future financial statements to be materially misstated, even though we have concluded that such adjustments are not material to the current financial statements. We proposed no audit adjustments that could, in our judgment, either individually or in the aggregate, have a significant effect on the Kellogg Arena Fund.

Disagreements with Management

For purposes of this letter, professional standards define a disagreement with management as a matter, whether or not resolved to our satisfaction, concerning a financial accounting, reporting, or auditing matter that could be significant to the general purpose financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the governmental unit's general purpose financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Issues Discussed Prior to Retention of Independent Auditors

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the Kellogg Arena Fund's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Difficulties Encountered in Performing the Audit

We encountered no difficulties in dealing with management in performing our audit.

This information and the attached memorandum is intended for the use of the City Council and management of the Kellogg Arena Fund and the State of Michigan. However, this report is a matter of public record, and its distribution is not limited.

Very truly yours,

A handwritten signature in black ink, reading "Lehmann Johnson". The signature is written in a cursive, flowing style with a large initial 'L' and 'J'.

CITY OF BATTLE CREEK KELLOGG ARENA FUND

COMMENTS AND RECOMMENDATIONS For the Year Ended June 30, 2005

During our audit we became aware of certain matters that are opportunities for strengthening internal control and operating efficiency. This memorandum summarizes our comments and recommendations regarding those matters, and does not affect our report dated September 2, 2005, on the financial statements of the City of Battle Creek Kellogg Arena Fund.

We will review the status of these comments during our next audit engagement. We have already discussed these matters with management and we will be pleased to discuss them in further detail at your convenience, to perform any additional study of these matters, or to assist in implementing the recommendations.

Internal Controls – Segregation of Duties

Management is responsible for establishing and maintaining effective internal control over financial reporting and the safeguarding of the City's assets. In establishing appropriate internal controls, careful consideration must be given to the cost of a particular control and the related benefits to be received. Accordingly, management must make the difficult decision of what degree of risk it is willing to accept, given the government's unique circumstances.

As is the case with many organizations of similar size, the City lacks a sufficient number of accounting personnel in order to ensure a complete segregation of duties within its accounting function. Ideally, no single individual should ever be able to initiate a transaction, record the transaction in the accounting records, maintain custody of the assets resulting from the transaction, and have continued access to the accounting records. Effectively, proper segregation of duties is intended to prevent an individual from committing an act of fraud or abuse and being able to conceal it.

Events of recent years have given rise to a heightened awareness of the risks of fraud and abuse, especially in the governmental environment, where public accountability is at its highest. The purpose of internal controls is to provide reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are properly authorized and recorded. Any limitations on the effectiveness of a government's internal controls carries with it a greater risk of fraud and abuse.

Often, it is perceived by individuals, both inside and outside of an entity, that an audit of the financial statements performed in accordance with applicable professional standards is tantamount to an audit of that entity's internal control, that such a financial statement audit is itself an internal control, and that the auditor is responsible for detecting all fraud and abuse. This is not true, and both management and the governing body need to understand this in considering its internal control policies and procedures.

While there are, of course, no easy answers to the challenge of balancing the costs and benefits of internal controls and the segregation of duties, we would nevertheless encourage management to actively seek ways to further strengthen its internal control structure by requiring as much independent review, reconciliation, and approval of accounting functions by qualified members of management as possible.

**CITY OF BATTLE CREEK
KELLOGG ARENA FUND**

**COMMENTS AND RECOMMENDATIONS (Concluded)
For the Year Ended June 30, 2005**

In addition to the broad comments regarding segregation duties, there are two particular areas to which we would like to draw attention. First, procedures should be established and followed for an independent review and approval of all journal entries; currently, this is not performed at the time of entry or after-the-fact. Second, there is no evidence that bank reconciliations and/or cancelled checks are regularly reviewed by a person independent of the accounts payable / general ledger function. This is a very important procedure to prevent or detect fraud.

* * * * *